NATIONAL ASSOCIATION of REALTORS®

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July 9, 2019

The Honorable Mike Thompson
Chairman
U.S. House of Representatives
Select Revenue Measures Subcommittee
House Committee on Ways and Means
1136 Longworth House Office Building
Washington, DC 20515

The Honorable Adrian Smith
Ranking Member
U.S. House of Representatives
Select Revenue Measures Subcommittee
House Committee on Ways and Means
1136 Longworth House Office Building
Washington, DC 20515

Dear Chairman Thompson and Ranking Member Smith:

On behalf of the more than 1.3 million members of the National Association of REALTORS®, I am submitting for the hearing record the attached comments for your hearing entitled "How Recent Limitations to the SALT Deduction Harm Communities, Schools, First Responders, and Housing Values," which was held on June 25, 2019.

Sincerely,

John Smaby
2019 President, National Association of REALTORS®

EQUAL HOUSING OPPORTUNITY

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HEARING BEFORE THE

HOUSE WAYS AND MEANS

SELECT REVENUE MEASURES SUBCOMMITTEE

ENTITLED

"HOW RECENT LIMITATIONS TO THE SALT DEDUCTION HARM COMMUNITIES, SCHOOLS, FIRST RESPONDERS, AND HOUSING VALUES"

WRITTEN COMMENTS BY

THE NATIONAL ASSOCIATION OF REALTORS®

JUNE 25, 2019

Chairman Thompson, Ranking Member Smith, and members of the Subcommittee:

On behalf of the more than 1.3 million members of the National Association of REALTORS®[1], thank you for the opportunity to provide written comments for this important hearing on how the recent limitations on individual taxpayers deducting state and local tax (SALT) payments affect communities, schools, first responders, and housing values. These comments are limited to our view of how the SALT limits impact the tax incentives for purchasing and owning a home[2].

Federal policy has long recognized the proliferation of macroeconomic, social, and wealth building benefits brought about by homeownership. This is why the government has enacted various provisions over the years to encourage more homeownership in our society. This has especially been the case in the federal tax law, which has, since its inception, provided strong tax incentives to help facilitate the purchasing and owning a home by making it more affordable.

Over the years, federal tax incentives for purchasing and owning a home have taken several forms, including a first-time homebuyer tax credit, which was vitally important during the depths of the most recent housing crisis. However, the longest-running and largest tax incentives for home ownership by far in terms of impact on taxpayers have been the mortgage interest deduction (MID) and the deduction for property taxes.

From the inception of the modern Internal Revenue Code in 1913 until 1987, both of these deductions were essentially allowed without limit, as long as homeowners itemized their deductions. The Revenue Act of 1987 placed a $1 million cap on the amount of mortgage debt the interest of which could be deducted. Significantly, this limit was not adjusted for inflation.

At the time the limit was enacted into the tax law, relatively few homes in America had mortgages of more than $1 million. However, due to inflation and other factors, home prices increased, and those increases varied greatly throughout the Nation, and after some years the limit began to affect more and more home purchasers in those parts of the country with the highest housing prices.

By 2017, the cap was still well above the amount of most mortgages taken out throughout the U.S., but in some of the highest price housing markets, the limit was routinely breached, even for relatively modest homes. Thus, in those areas with the highest-priced homes, the mortgage interest deduction limit was already affecting many current and prospective homeowners, not because their homes were necessarily lavish or large, but in many cases simply because they happened to live in a higher-cost area.

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[1] *NAR's members are real estate professionals engaged in activities including real estate sales and brokerage, property management, residential and commercial leasing, and appraisal. The business approach of REALTORS® is a highly personal, hands-on, face-to-face model, focused on helping fulfill a family's fundamental need for shelter. NAR has long prided itself as a voice for not only its members, but for America's 78 million homeowners, as well as the tens of millions more Americans who aspire to own their home one day.*

[2] *We believe that the SALT limit has reduced home values in many areas of the Nation. However, much of our basis for this belief is anecdotal. Until more data is available for 2018, such as from the Internal Revenue Service, we believe it is better to focus on the SALT cap's impact on the tax incentives of homeownership.*

There are important parallels between the mortgage debt limit enacted in 1987 and the limit on SALT payments, which was included in the Tax Cuts and Jobs Act (TCJA) of 2017. Both have unindexed thresholds, both directly affect those who live in high-home-price areas much more than they affect those who do not, and both undermine the incentive effect for those who hope to move from renting to owning a home. Moreover, the mortgage debt limit was lowered in the TCJA to just $750,000, further exacerbating the effects of these limits for current and future homeowners.

In areas of the Nation where home prices are higher, the new $750,000 mortgage limit has had an immediate and negative effect for many who borrowed to purchase their home. A similar negative impact can also be found in the new $10,000 SALT deduction limitation. In this case, the new tax reform act represents the first encroachment on full deductibility of real estate taxes. As with the MID change, however, the new limit is largely regional in its impact, as most homeowners throughout the U.S. fall far below the $10,000 limit for all state and local taxes, at least for the immediate future.

As with the old and new MID mortgage limits, the new SALT limitation was not indexed for inflation. So, as taxes naturally rise with inflation and other factors, more and more current and prospective homeowners will be caught by the new cap and will see the amount of tax benefits of owning a home go down, which in turn will force the cost of owning a home go up.

Despite the fact that much of the nation is not immediately affected by the new changes on MID and the property tax deduction, the case remains that millions of homeowners in the higher-housing-cost areas of the Nation will be negatively impacted by the changes. And many of these will be members of the middle-class living in homes that are far from large and lavish.

The new SALT limit also discourages marriage and encourages divorce. This is because it offers the same $10,000 limit for both single individuals and married couples filing a joint return. Such a result flies in the face of the kind of pro-family public policy embraced by both sides of the political aisle.

The effects of the TCJA changes described thus far are quite straightforward. However, a more obscure but much more damaging result from the SALT cap exists in its impact on the basic access to the tax benefits of buying and owning a home. Here we are talking about the SALT limit's interaction with the higher standard deduction, which was also a feature of the Tax Cuts and Jobs Act. And unfortunately, this impact is not felt just by those who live in higher-housing-cost areas, but is instead focused on current and potential homeowners of more moderate incomes in every region.

By nearly doubling the standard deduction, the TCJA reduced some of the complexity of the tax system. But for many, it also eviscerated the incentive value of itemized deductions that are meant to encourage certain behavior, such as purchasing and owning a home. This is because unless the actual amount of itemized deductions exceeds the new, higher amount of the standard deduction, the expenditure that gave rise to the itemized deduction, such as paying mortgage interest or property taxes, has no incentive value. Thus, for those who do not itemize, owning a home is the tax equivalent to renting one, as there is no additional tax benefit.

This effect is not new. Taxpayers with actual itemized deductions below the standard deduction level always found their itemized deductions to be meaningless. However, what is new is the unprecedented jump in the standard deduction included in the TCJA. For tax year 2017, before the changes made by the new tax reform act took effect, about 32 percent of tax filers itemized their deductions[3]. In other words, almost one in three taxpayers could access the tax benefits of purchasing a home. Further, it was often the act of purchasing that first home that put a tax filer's total itemized deductions over the standard deduction amount, thereby giving meaning to the incentives of the MID and property tax deduction, which acted to reduce the home buyer's tax liability and provide a tax incentive to own rather than rent.

However, for tax year 2018, when the higher standard deduction amounts are in effect, only about 13 percent, or about one in eight taxpayers, were expected to elect to itemize their deductions[4]. This means, of course, that seven of eight taxpayers will claim the standard deduction and will find no incentive effect of the MID and property tax deduction. While some few of these who are not homeowners will find that purchasing a home would increase their itemized deductions to a level higher than the standard deduction and thus enter the range where the MID and property tax could lower their tax liability vis-à-vis renting, the numbers who do so will be very low as compared to those who could enjoy these incentives before the tax reform law changes went into effect.[5]

It is also vital to note that this effect has been exacerbated for many by the new SALT limit. By limiting the SALT deduction of millions of current and potential homeowners to $10,000, it will become much more difficult for many of them to have their itemized deductions exceed the standard deduction level so they become meaningful and begin to reduce their tax liability.

In other words, the huge increase in the standard deduction itself only tells part of the story in the greatly reduced number of itemizers. Some have become standard deduction claimants because the new threshold for claiming this status now exceeds the amount of their itemized deductions. But for many others, those itemized deductions have gone down to below the level of the standard deduction by reason of the SALT cap.

What is important to note is that eliminating or raising the SALT limit, even without lowering the standard deduction, would again activate the incentive power of the MID and property tax deduction for many current and prospective homeowners. Of course, the higher the cap is raised, the more meaningful the itemized deductions once again become.

Conclusion

While federal tax policies designed to reduce the cost of purchasing and owning a home by making that home more affordable are still present in the current law, they have been

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[3] *Overview of the Federal Tax System and Policy Considerations Related to Tax Reform, Joint Committee on Taxation, JCX-36-17, July 14, 2017, page 4.*

[4] *Overview of the Federal Tax System as in Effect for 2018, Joint Committee on Taxation, JCX-3-18, February 7, 2018, page 4.*

[5] *It is important to note that the Tax Cuts and Jobs Act will, in many cases, lead to a lower tax liability for those who will no longer be itemizing their deductions. This is especially true if the tax filer can claim the newly-increased credit for children under age 17. However, that lower tax liability will often be available whether the filer owns a home or rents one and the incentive effect of the tax benefits of homeownership will be decreased or nullified.*

significantly reduced and are a fraction of what they were just one year before the effective date of the Tax Cuts and Jobs Act. Such policies can still be considered benefits for those who are fortunate enough to still be able to enjoy them. However, for the large number of current and would-be middle-class homeowners who are no longer able to claim these benefits, the changes in the Tax Cuts and Jobs Act amounts to a significant barrier to homeownership.

The SALT limit has become the subject of a great amount of heated partisan debate. The National Association of REALTORS® supports an unlimited SALT deduction. The limit has impeded the value of the long-standing tax incentives of home ownership in both a direct and indirect way. However, it is important for the Subcommittee and indeed all Members of Congress to understand that just raising the cap significantly, by correcting the marriage penalty[6], for example, would go a long way toward making the homeownership tax incentives meaningful for millions of people who no longer benefit from their intended value.

[6] *Specifically, the SALT limit marriage penalty should be corrected by doubling the allowable deduction to $20,000 for married couples filing a joint return. We also highly recommend the SALT deduction limits be indexed for inflation.*